

Internal Revenue Service
memorandum

TL-N-5379-89

TS/CTSANDERSON

date: **JUN 30 1989**

to: District Counsel, Sacramento W:SAC

from: Assistant Chief Counsel (Tax Litigation) CC:TL

subject: Post-Review of Advisory Opinion Regarding
TEFRA and California Limited Partnership
Registration Requirements

This memorandum is in response to your request that we post review your advisory opinion to Sacramento Examination dated March 28, 1989. Your advisory opinion covered the following issues.

ISSUES

1. Are there California registration requirements that apply to a California limited partnership?
2. If such registration requirements exist but are not satisfied, can a California limited partnership be created?
3. How does the classification of a partnership as general or limited affect the designation of a tax matters partner?

CONCLUSION

We agree with your discussion of the issues above with one exception. On page 5 of your opinion, you state National Office position as: In determining whether a partner is a general or limited partner for purposes of selecting the tax matters partner, the Service should rely only on the certificates filed with the appropriate state offices and the subscription agreements, and cannot rely on the filed Forms 1065 and Schedules K-1. This statement is in part too narrow and in part incorrect. Once the partnership is classified as limited, all facts and

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circumstances that are relevant should be considered in determining which partners are limited partners and which are general partners. Of course, the certificate of limited partnership is highly probative with respect to this question. The subscription agreements may also be relevant. However, other documents should prove to be more helpful than the subscription agreements, particularly the partnership agreement. Furthermore, the 1065s and K-1s for the applicable years would be relevant, though not necessarily solely determinative. Conflict between any of these documents should be resolved on a case by case basis, with assistance available from the National Office if necessary.

DISCUSSION

Your advisory opinion concerns the California registration requirements for limited partnerships and their relationship to the designation of a tax matters partner. The purpose of the opinion was to provide to Sacramento Examination general information for inclusion in a TEFRA tax matters partner checklist pertaining to California limited partnerships. (A copy of the opinion is attached.)

As you correctly state, Federal law determines whether there is a partnership. Frazell v. Commissioner, 88 T.C. 1405, 1412 (1987). Federal law also determines when a partnership is formed. Frazell v. Commissioner, *supra*; Sparks v. Commissioner, 87 T.C. 1279, 1282 (1986). The determination of whether the partnership is a limited or general partnership, however, is to be made under state law criteria. See Frazell v. Commissioner, *supra* at 1413. Similarly, state law criteria generally governs the determination of whether a person is a partner and, if so, whether he is a general or limited partner. See I.R.C. § 6231(a)(2)(A) ("partner" means . . . a partner in the partnership"). But compare I.R.C. § 6231(a)(2)(B) (A "partner" for TEFRA purposes can include "any other person [though technically not a partner] whose income tax liability . . . is determined in whole or in part by taking into account directly or indirectly partnership items of the partnership.")

If under the applicable state law a limited partnership is not effectively created, the partnership is a general partnership (assuming it is a partnership in the first instance), and all its partners are general partners. Since California's limited partnership act (both pre-July 1, 1984 and post-June 30, 1984) requires that a certificate of limited partnership be filed before a limited partnership is deemed to exist, failure to file a certificate prohibits the partnership from being a limited partnership during the period of non-filing. Since the partnership is not a limited partnership during the period of non-filing, none of the partners can be considered limited

partners during such period, i.e., they all are general partners. The purported limited partners of such a partnership are general partners even though they may be given some attributes of limited liability under the California statute, as you point out in footnote 2, page 3 of your advisory opinion.

As a general rule, only general partners can be tax matters partners (TMPs). Therefore, the determination of whether a partner of a limited partnership is a limited or general partner is essential to the question of whether an appropriate partner has been designated as TMP by the partnership under section 6231(a)(7)(A), which allows only general partners to be so designated. See Temp. Treas. Reg. 301.6231(a)(7)-1T. This determination is also essential in applying the "largest profits interest" rule in selecting a "general partner" as TMP in the absence of a designation by the partnership, pursuant to section 6231(a)(7)(B). Id. See also Rev. Proc. 88-16, 1988-1 C.B. 691. Finally, this determination must also be made in selecting a partner as TMP under Rev. Proc. 88-16, when application of the "largest profits interest" rule proves impracticable. (This procedure allows for selecting a limited partner as TMP, but only in situations where all general partners are unsuitable for selection.)

Our one correction to your opinion concerns your statement about National Office position on what evidence should be relied on in determining whether a partner is a general or limited partner for purposes of selecting the tax matters partner. On page 5 of your opinion, you state National Office position as: In determining whether a partner is a general or limited partner for purposes of selecting the tax matters partner, the Service should rely only on the certificate filed with the appropriate state offices and the subscription agreements, and cannot rely on the filed Forms 1065 and Schedules K-1. This statement is in part too narrow and in part incorrect.

Once the partnership is classified as limited, all facts and circumstances that are relevant should be considered in determining which partners are limited partners and which are general partners. Of course, the certificate of limited partnership is highly probative with respect to this question. The subscription agreements may also be relevant. However, other documents should prove to be more helpful than the subscription agreements, particularly the partnership agreement. Furthermore, the 1065s and K-1s for the applicable years would be relevant,

though not necessarily solely determinative. 1/ Conflict between any of these documents should be resolved on a case by case basis, with assistance available from the National Office if necessary.

If you have any questions, contact Ted Sanderson on (FTS) 566-3233.

MARLENE GROSS

By:

Kathleen E. Whatley
KATHLEEN E. WHATLEY
Chief, Tax Shelter Branch

Attachment:
As stated.

1/ You distinguish the Harrell and Z-Tron cases in concluding that the Service cannot rely on the 1065 or K-1s in determining whether a partner is a general or limited partner. We agree that the Harrell and Z-Tron holdings do not mandate that the Service strictly rely on the 1065 and K-1s in making this determination. See Z-Tron Computer Research and Development Program v. Commissioner, 91 T.C. 258 (1988), Harrell v. Commissioner, 91 T.C. 242 (1988) (held that, in determining whether a partnership is a small partnership and whether the same share rule is satisfied, the Service can rely solely on the partnership return and K-1s). However, the 1065 and K-1s certainly are relevant to the inquiry of whether a partner is general or limited. In fact, in certain situations the Service may want to rely on Harrell and Z-Tron to argue that sole reliance on the 1065 and K-1s in determining the TMP to whom the FPAA should be sent was justified. For example, such a situation may exist when there was not sufficient time to review the other relevant documents mentioned above before the period for issuing the notice of FPAA expired.